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In the Matter of

Applications of America Online, Inc.
and Time Warner, Inc. for
Transfers of Control

CS Docket No. 00-30

WRITTEN EX PARTE FILING OF THE WALT DISNEY COMPANY

**THE COMMISSION SHOULD NOT APPROVE THE AOL/TIME WARNER
COMBINATION WITHOUT IMPOSING STRONG AND ENFORCEABLE
CONDITIONS TO SAFEGUARD AGAINST ANTICOMPETITIVE AND ANTI-
CONSUMER CONDUCT BY THE MERGED ENTITY**

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TABLE OF CONTENTS

I.	INTRODUCTION AND OVERVIEW	1
II.	THE INTERNET TODAY	7
A.	THE INTERNET HAS RAPIDLY BECOME A MAJOR ECONOMIC AND CULTURAL FORCE	7
B.	THE ESSENCE OF THE INTERNET HAS BEEN ITS OPENNESS	8
III.	AOL ALREADY IS THE DOMINANT COMPANY ON THE INTERNET	9
A.	AOL TODAY	9
B.	AOL'S POSITION IS STRENGTHENING	11
C.	AOL HAS SUBSTANTIAL POWER IN SEVERAL INTERNET MARKETS	13
D.	AOL OBTAINED AND HAS MAINTAINED ITS DOMINANT POSITION THROUGH EXCLUSIONARY CONDUCT	17
IV.	TIME WARNER POSSESSES ENORMOUS MARKET POWER.....	20
A.	TIME WARNER HAS SUBSTANTIAL MARKET POWER AT BOTH THE DISTRIBUTION AND PROGRAMMING LEVELS OF THE CABLE INDUSTRY.....	20
B.	TIME WARNER'S LOCAL CABLE MONOPOLIES GIVE IT ENDURING MARKET POWER	21
C.	TIME WARNER IS THE WORLD'S LARGEST TRADITIONAL MEDIA COMPANY	22
D.	THE BREADTH OF TIME WARNER'S HOLDINGS PLACES IT IN A UNIQUE POSITION TO DOMINATE THE INTERACTIVE SERVICES MARKET	24
E.	TIME WARNER'S EXCLUSIONARY CONDUCT	24
F.	TIME WARNER'S EXERCISE OF MONOPSONY POWER.....	30
G.	AOL AND TIME WARNER'S PATTERN OF ABUSE THREATENS THE INTERACTIVE TELEVISION MARKET.....	31
V.	INTERACTIVE TELEVISION IS RAPIDLY EMERGING AS THE FUTURE OF TELEVISION.....	31
VI.	THERE WILL BE NO CLOSE SUBSTITUTES FOR CABLE IN THE PROVISION OF INTERACTIVE TELEVISION FOR THE FORESEEABLE FUTURE	34

VII.	PAST IS PROLOGUE: AOL/TIME WARNER WILL HAVE THE ABILITY AND INCENTIVE TO USE EXCLUSIONARY POWER IN THE INTERACTIVE TELEVISION MARKET.....	37
A.	MEDIA INCUMBENTS HAVE LONG USED THEIR POWER TO EXCLUDE RIVALS IN EMERGING MARKETS.....	37
B.	PRE-MERGER INCENTIVES FOR AN OPEN INTERACTIVE TELEVISION SYSTEM OUTWEIGH THE INCENTIVES FOR A CLOSED SYSTEM.....	40
C.	POST-MERGER AOL/TIME WARNER WOULD HAVE THE INCENTIVE AND THE ABILITY TO CLOSE THE INTERACTIVE TELEVISION SYSTEM	43
D.	THE AOL-TIME WARNER CLOSED SYSTEM WILL SPREAD BEYOND TIME WARNER'S CABLE SYSTEMS.....	45
E.	CONSUMERS WOULD BE HARMED BY THE CLOSED INTERACTIVE TELEVISION SYSTEM.....	46
F.	AOL-TV: THE SHAPE OF ANTICOMPETITIVE AND ANTI-CONSUMER BEHAVIOR FROM AOL/TIME WARNER TO COME.....	48
VIII.	THE COMMISSION CANNOT APPROVE THE AOL/TIME WARNER ACQUISITION UNLESS IT DETERMINES THAT IT IS IN THE PUBLIC INTEREST AND PROCOMPETITIVE.	50
IX.	CONDITIONS THE COMMISSION SHOULD IMPOSE AS A PREREQUISITE TO ANY APPROVAL OF THE AOL/TIME WARNER ACQUISITION.....	53
A.	THE COMMISSION SHOULD REQUIRE AOL/TIME WARNER TO SEPARATE ITS OWNERSHIP OF CONTENT FROM ITS OWNERSHIP OF ITS BROADBAND CABLE DISTRIBUTION FACILITIES.....	53
B.	IN THE EVENT THE COMMISSION DOES NOT REQUIRE SEPARATE OWNERSHIP OF THE BOTTLENECK CONDUIT AND THE CONTENT FLOWING OVER IT, THE COMMISSION SHOULD IMPOSE CLEAR AND ENFORCEABLE CONDITIONS ON ANY APPROVAL OF THE AOL/TIME WARNER ACQUISITION PROHIBITING DISCRIMINATION AGAINST UNAFFILIATED CONTENT AND INTERACTIVE TELEVISION SERVICE PROVIDERS.	60
C.	SOURCES AND PRECEDENTS FOR ANTI-DISCRIMINATION CONDITIONS.....	63
D.	ANTI-DISCRIMINATION CONDITIONS NEEDED TO MITIGATE THE ANTICOMPETITIVE EFFECTS OF THE AOL/TIME WARNER ACQUISITION.....	66
E.	THE COMMISSION SHOULD REQUIRE INTEROPERABILITY AMONG AOL/TIME WARNER INSTANT MESSENGERS AND RIVAL INSTANT MESSENGERS.....	80

X.	ARBITRATION PROCEDURES SHOULD BE USED TO ENFORCE THE SAFEGUARDS NECESSARY TO PREVENT AOL/TIME WARNER FROM ENGAGING IN ANTICOMPETITIVE, DISCRIMINATORY BEHAVIOR IN THE INTERACTIVE TELEVISION SERVICES MARKET.	81
XI.	SUMMARY OF PROPOSED TEXT OF CONDITIONS THAT SHOULD BE IMPOSED ON THE AOL/ TIME WARNER MERGER.....	82
A.	CONDITION MANDATING SEPARATE OWNERSHIP OF BOTTLENECK BROADBAND CABLE CONDUIT AND ITS CONTENT TO ENSURE COMPETITION AND CONSUMER CHOICE IN THE INTERACTIVE TELEVISION SERVICES MARKET.	82
B.	STRUCTURAL SAFEGUARDS ABSENT COMPLETE SEPARATION OF CONTENT AND CONDUIT.....	82
C.	IN THE ALTERNATIVE, CONDITIONS TO ENSURE NON-DISCRIMINATION, COMPETITION, AND CONSUMER CHOICE IN THE INTERACTIVE TELEVISION SERVICES MARKET.	83
XII.	CONCLUSION	85

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I. INTRODUCTION AND OVERVIEW

The \$183 billion acquisition¹ by America Online, Inc. ("AOL") of Time Warner, Inc., the largest merger in corporate history, threatens the ability of U.S. consumers to access freely a new and revolutionary product, Interactive Television. The merger will allow AOL to leverage its dominant position in online Internet services with Time Warner's local cable monopolies to control the emergent Interactive Television market.

AOL already is, without question, the dominant provider of online Internet services to residential subscribers. AOL, as its President points out, is "uniquely positioned in the Internet industry" with "an unparalleled connection to consumers."² The fact that AOL's 23 million subscribers spend 85 percent of their time within its "walled garden," rather than the Internet at large, speaks volumes about the extent of AOL's market power and the ability to exclude competition. Time Warner, of course, not only has extensive publishing, television, film, and

¹ *Welcome to the 21st Century*, BUSINESSWEEK, Jan. 24, 2000, at 37.

² See AOL Third Quarter Earnings Report, <<http://corp.aol.com/investors.shtml>> ("AOL Earnings Report").

music holdings making it “the world’s leading media company,”³ but also controls bottleneck cable pipelines in communities encompassing 20 percent of the U.S. population. The merged company will be “the driving force behind the next wave of online consumer usage growth and the continued convergence of the Internet and television.”⁴

The Walt Disney Co. (“Disney”) is a diversified worldwide entertainment company engaged in the creation and marketing of entertainment content, including live-action and animated motion pictures, broadcast and cable television programming, musical recordings, and a wide variety of online content and services. For Disney to succeed in entertaining people of all ages, consumers must have unhindered access to its creative products. Disney’s concern is that the combination of AOL and Time Warner will significantly augment each company’s respective bottleneck monopolies over the distribution of news, information and entertainment content, thereby increasing the combined company’s ability and incentive to engage in exclusionary behavior at multiple levels of broadband content and distribution.⁵

The acquisition’s likely anticompetitive effects are especially acute because it is occurring just as the video marketplace is undergoing a major revolution: the three-way convergence of traditional television, Internet services, and broadband delivery to create an entirely new product, Interactive Television. Industry analysts predict that by 2005, Interactive

³ See Time Warner Inc., *About Time Warner* (visited 7/17/2000) <<http://www.timewarner.com/corp/about/timewarnerinc/corporate/index.html>>.

⁴ See LEHMAN BROTHERS, *AMERICA ONLINE 2* (2000) (“Lehman Brothers Report”).

⁵ In marked contrast, the transmission of free over-the-air broadcasting by ABC in a media universe of seven broadcast networks, more than 100 cable/satellite networks and 1500 commercial television stations does not involve bottleneck control such as can be exercised through the operation of a closed cable platform, and arguments attempting to equate the two are unavailing.

Television will reach 24 million households,⁶ earning revenues of more than \$25 billion.⁷ This emerging Interactive Television market, like the Internet of the late 1990s, is likely to demonstrate explosive creativity and innovation if permitted to develop in an open and competitive fashion. On the other hand, Interactive Television will most certainly fall short of its remarkable potential if it is controlled by a vertically-integrated gatekeeper with the ability and incentive to exclude competition and restrict consumer choice.

Disney believes that a combined AOL/Time Warner will undermine the development of an open-platform Interactive Television market. A videotape, "Consumer Choice In the Broadband Marketplace Of Tomorrow," filed as Exhibit A to this submission, depicts how this is likely to occur. AOL already has introduced an Interactive Television platform that leverages its position as the dominant online service provider ("OSP") but, at least pre-acquisition, its incentives were to develop an open standard that would encourage multiple source development of new Interactive Television programming. Once it takes ownership of Time Warner's cable pipeline and programming assets, however, AOL's post-acquisition incentives would be to create a partially closed system by discriminating against third-party programming. The ownership of programming and the set-top operating system may be enough to enforce the closure of the system. But if it were not, the addition of Time Warner's cable monopolies to AOL's portfolio surely would provide the bottleneck necessary to enforce closure. With all the pieces in place, AOL/Time Warner would have the ability and incentive to foreclose independent and competitive development of Interactive Television. Such foreclosure is particularly ominous

⁶ See FORRESTER RESEARCH, INTERACTIVE TV CASH FLOWS (1999).

⁷ See Ken Kerschbaumer, *Fulfilling the Promise: The Cable Industry Is Poised To Capitalize on the Concept's Long-Awaited Potential*, BROADCASTING & CABLE, July 10, 2000, at 22 (reporting Meyers Group estimate).

because Interactive Television is poised for explosive development, and this merger will shrink rather than expand consumer access to independent voices, undermining First Amendment values.

This stifling of independent programming for Interactive Television will in turn strengthen the combined company's cable monopolies, as AOL/Time Warner would have the incentive to protect those monopolies by denying cable overbuilders and other multichannel video programming distributors access to interactive programming. In addition, the company will be able to leverage its Interactive Television programming clout into non-Time Warner cable territories by offering incumbent cable operators a Faustian bargain: take our Interactive Television programming and set-top operating system, and we will deny your competitors the same.⁸ The resulting Interactive Television landscape will be characterized by three-level entry barriers; any potential entrant into the cable delivery, set top operating system, or interactive programming markets would have to enter *all three markets* simultaneously to overcome the gatekeeper.

The foregoing anticompetitive effects might be considered speculative if AOL and Time Warner had demonstrated a propensity for openness by operating open and competitive systems in their respective fields. Nothing, however, could be further from the truth. AOL has successfully closed its online services, creating a "walled garden" from which users find it difficult to escape. The company has accomplished this through restrictive contracts that prohibit or limit hyperlinks, interfering with the link-to-link web surfing that previously had

⁸

For the country's largest cable operator, AT&T, Time Warner can offer an additional incentive: granting AT&T's wish to provide local telephone service via Time Warner's cable systems, as the companies have already agreed on a preliminary basis.

embodied the Internet. Similarly, AOL has purposefully obstructed interoperability between its two instant messaging systems and competitive systems. AOL has not done this by simply refusing to deal; rather, it has actually created incompatibilities to prevent such interoperability.

Time Warner's notorious exclusionary acts have been front-page news. Time Warner continually threatened Disney when Disney attempted to offer free satellite dishes to cable subscribers as an alternative to Time Warner's cable monopoly. When private threats and public vilification were not enough, Time Warner simply took Disney's ABC owned and operated television broadcast stations off its cable systems without prior notice. Time Warner also squelched competition in the electronic programming guide market by preventing Gemstar from operating its programming guide, which competed with Time Warner's own programming guide, in Time Warner's cable territories. Again, this was not simply a monopolist's refusal to deal because Time Warner had to purchase and deploy special equipment to block Gemstar's competing service. There are many other examples of Time Warner's exclusionary practices that favor its own programming, such as refusing to carry certain local news services and providing preferred channel positions to its own programming. Recently, AOL and Time Warner have engaged in a self-serving effort to mitigate the harm they have caused with admissions of wrongdoing and apparent or partial reversals of exclusionary conduct as this merger comes under increasing scrutiny. However, these transparent flip-flops remain hollow and unenforceable, evidencing that AOL and Time Warner will do anything short of adhering to enforceable law to see this merger approved by the Commission.

AOL's and Time Warner's individual proclivities to foreclose and exclude competition will have adverse consequences for the development of Interactive Television. The combined company will bring to bear all of the exclusionary tools necessary to assure that Interactive

Television does not threaten AOL's dominance of the Internet or Time Warner's dominance of local cable markets. The result of these developments will be the loss of an open market for Interactive Television. Instead, there will be a closed system with less choice, less innovation, lower quality and higher prices. In essence, it will be the loss of that end-to-end freedom that so quickly has made the Internet (and Interactive Television will be a crucial component of Internet usage for residential customers) such a vibrant part of American society.

Disney urges the Commission to ensure that the proposed merger does not produce such an anticompetitive result. The surest remedy would be a separation of content from distribution, as has been required in the past when there has been bottleneck monopoly power in distribution of entertainment and news media. Failing that, the Commission should impose meaningful and enforceable anti-discrimination provisions. To facilitate enforcement of such terms, the Commission should require the merged firm to hold its content and distribution services in separate affiliates, a minority stake in one of which should be sold to an independent party both to act as a monitor and to create incentives for arm's length dealing. In addition, as has been done in many other cases, the Commission should give private parties a right to enforce the provisions of the Commission's order through arbitration, thereby expediting dispute resolution and reducing the administrative burden on the Commission.

The potential for irreversible and irreparable anticompetitive harm to the public flowing from the AOL/Time Warner merger is so great and so predictable that the Commission cannot wait to determine how the market develops. Meaningful and enforceable conditions must be imposed now before the arsenal of anticompetitive weapons available to the merged company is assembled and integrated into a closed, Interactive Television systems architecture. Appropriate prophylactic measures instituted as a condition of any Commission approval of the AOL/Time

Warner combination are indispensable to consumers having access to diverse sources of news, information and entertainment over the AOL/Time Warner cable broadband platform. Without such conditions, competition and consumer choice in the emerging Interactive Television market will be foreclosed. American consumers will be the victims.

II. THE INTERNET TODAY

A. THE INTERNET HAS RAPIDLY BECOME A MAJOR ECONOMIC AND CULTURAL FORCE

From its modest beginnings as a research project developed by DARPA, the Internet has grown into an incredible network connecting people across the world and causing economic change at an unparalleled pace. No longer a tool of academic and research institutions, people of all types and ages are plugging into the World Wide Web. In the week ending July 2, 2000, nearly 60 million Americans actually used the Internet.⁹ Regular users are likely to spend at least one hour online at a time.¹⁰

Millions of U.S. users are utilizing their access as they never have in the past. Today, the Internet has gone beyond the bounds of its earlier title of the "information superhighway." It has become a virtual marketplace, where the user can buy anything from the latest best seller to a used car, and this trend has not gone unnoticed by U.S. companies.

As technology makes accessing the Internet quicker and easier to use, the numbers are expected to rise in nearly every category. More than 50 percent of U.S. households are expected to have Internet access by 2001, with one in three having purchased goods or services online.¹¹

⁹ See Nielson/NetRatings Reporter, July 7, 2000, < <http://63.140.238.20/weekly.asp>>.

¹⁰ Nau, *Internet Surveys* (visited July 6, 2000) <<http://www.nau.ie/surveys/index.cgi>> (citing AC Nielsen report).

¹¹ See Nau, *Internet Surveys* (visited June 1, 2000) < http://www.nua.ie/surveys/index.cgi?f=FS&cat_id=34> (citing Forrester Research study).

In 1999, businesses realized combined revenue of \$33.1 billion from Internet sales to the consumer.¹² By the end of 2000, this number will likely nearly double to \$61 billion.¹³ The growing numbers of people jumping on the World Wide Web also will increase ISP revenue from \$17.7 billion in 1999 to a projected \$60.5 billion by 2004.¹⁴

B. THE ESSENCE OF THE INTERNET HAS BEEN ITS OPENNESS

From its beginning, a major distinguishing factor of the Internet, as compared to other networks, has been its openness and freedom.¹⁵ Cyberspace was built through the voluntary efforts of thousands of individuals, building upon the efforts of those who have gone before. The result has been a wondrously mutating entity that has emerged and changed extraordinarily rapidly. As a result, tens of millions of people have gained virtually instantaneous access to undreamed quantities of data of their own choosing, as well as the ability to communicate their own thoughts to a worldwide community.

However, it is not inevitable that the freedom that has characterized the Internet to date will continue. Stanford University Law Professor Lawrence Lessig argues persuasively that as the Internet further develops into a sphere for commerce, it is becoming a highly regulable space.¹⁶ Choices made by private entities and governments will determine whether the Internet

¹² See Boston Consulting Group, *New BCG Ideas* <http://bcg.com/new_ideas/new_ideas_splash.asp>.

¹³ See *id.*

¹⁴ See AllNet Research Report, *Internet Service Provider Market Review and Forecast, 1999-2004* (visited July 11, 2000) <<http://allnetresearch.internet.com/reports/isprev/index.html>>.

¹⁵ This is not to suggest that content on the Internet should be made available free of charge, a notion that might be confused with freedom of consumer choice and the ability to place content on the Internet without unreasonable restrictions.

¹⁶ See LAWRENCE LESSIG, *CODE AND OTHER LAWS OF CYBERSPACE* 30-32 (1999).

will retain its present day end-to-end freedom. Left entirely to private action, it is likely that gatekeepers will develop who will push the Internet into constricted channels.

This is precisely the intention of AOL with its “walled garden” philosophy. It also is a prospect much more likely to occur if the acquisition of Time Warner is allowed to consummate without government action to protect the freedom of choice and access of Internet users and interactive TV viewers. As Professor Lessig puts it, the basic assumptions of the Internet “were grounded in liberty and openness. An invisible hand now threatens both.”¹⁷ As we will show below, the invisible hand is now visible and the threat is immediate. It is the AOL/Time Warner acquisition.

III. AOL ALREADY IS THE DOMINANT COMPANY ON THE INTERNET

A. AOL TODAY

AOL “is uniquely positioned in the Internet industry” with “an unmatched collection of interactive brands” and “an unparalleled connection to consumers,” according to its President and Chief Operating Officer, Bob Pittman.¹⁸ Or, as a recent analyst report puts it, “AOL’s Leadership in Cyberspace is Insurmountable.”¹⁹

AOL’s flagship AOL service has over 23 million subscribers,²⁰ CompuServe 2.7 million

¹⁷ See *id.* at 60.

¹⁸ See AOL Earnings Report.

¹⁹ See Lehman Brothers Report, at 2.

²⁰ Remarks of Stephen M. Case, AOL Chairman and CEO at Special Stockholders Meeting, June 23, 2000 <<http://www.timewarner.com/corp/about/timewarnerinc/corporate/speeches.html>>.

and AOL's Gateway.net service 850,000;²¹ 26 million subscribers in all.²² AOL also controls many other leading Internet brands or applications which, in combination, give it "unparalleled operating leverage."²³ Key among these are:

- AOL Instant Messenger ("AIM") and AOL Buddy List services with 91 million registrants and AOL's ICQ instant messaging service with 62.4 million users, for a combined total of over 153 million users. The average ICQ user keeps it on the desktop nearly three hours per day.²⁴
- AOL.com and Netscape Netcenter, two leading Internet portals, are under AOL's control. According to one recent analyst report, AOL.com has nearly 32 million unique monthly visitors, while Netscape Netcenter had almost 20 million unique visitors.²⁵ Netcenter has more than 28 million registered users.²⁶
- Spinner and WINamp, leading Internet music properties with 20 million customer relationships.²⁷ WINamp is the number one favorite music player with more than 25 million unique registrations, and the two sites combined reach ten million unique users each month.²⁸
- Digital City, the leading local online network, with more than five million unique visitors in May, 2000. Digital City has expanded to 220 markets and has more than 2,000 partners. Its estimated revenues are more than seven times those of its nearest competitor, TicketMaster-City Search.²⁹

²¹ See AOL Earnings Report.

²² See Lehman Brothers Report, at 2.

²³ *Id.*

²⁴ See Remarks of Bob Pittman, President and Chief Operating Officer, America Online, Inc., AOL Third Quarter Conference Call, April 18, 2000 <<http://corp.aol.com/conf00q3.html>>.

²⁵ See Media Metrix, *Digital Media Key Measures* (electronic edition), April, 2000.

²⁶ See AOL Press Release, *America Online Poses Record Earnings*, April 18, 2000 <<http://media.web.aol.com/media/press.cfm?>>.

²⁷ See JEFFERIES & COMPANY, INC., AMERICA ONLINE, INC. 6 (2000) ("Jefferies Report").

²⁸ See AOL Earnings Report.

²⁹ See Lehman Brothers Report, at 41.

- AOL MovieFone, the nation's largest online movie listing³⁰ guide and ticketing service, which attracts 20 percent of all moviegoers.
- MapQuest.com which delivers more than 150 million maps and driving instructions each month. In May 2000, MapQuest had more than 5.7 million unique visitors and was the largest directions-related site on the Internet.³¹
- Netscape Communicator client software,³² including the Netscape Navigator browser that claims 70 million users.

Through its family of brands, AOL "now has an unduplicated reach of roughly 80 percent of all Internet users in the United States, by far the greatest on the Web."³³

B. AOL'S POSITION IS STRENGTHENING

The description of AOL above is a snapshot in time. What is perhaps more significant is the exponential growth of AOL, which quickly is growing the company's already substantial market power. Subscription to AOL's flagship service has grown from 1 million in 1994 to 23 million today, with an increase of 2.5 million so far in 2000 alone. The paying membership base across AOL's family of brands is likely to increase by 6 million per year over the next two years.³⁴ Average time online was 64 minutes in AOL's Third Quarter, up 16 percent on a year-to-year basis.³⁵ In the last three years, AOL's usage has increased from 6 to 33 hours per

³⁰ See AOL Earnings Report.

³¹ See Lehman Brothers Report, at 45.

³² See Jefferies Report, at 6.

³³ See Lehman Brothers Report, at 22.

³⁴ See *id.*, at 5.

³⁵ See AOL Earnings Report.

month.³⁶ The Netscape Netcenter portal doubled its total of a year ago to 28 million users today.³⁷

The explosion in AOL's instant messaging services is even greater, with the AIM and Buddy List service increasing by 21 million registrants in the most recent quarter, from 70 to 91 million, and with the ICQ service adding 9.3 million registrants, bringing AOL's total instant messaging registrants to over 153 million. In the last quarter, AIM also launched its version 4.0, which allows voice communications and Instant Images, which allows users to exchange images and sounds.³⁸

AOL also is moving rapidly toward implementing its "AOL Anywhere" goal on "multiple fronts – from wireless to broadband content, Internet appliances to AOL TV."³⁹ In the last quarter alone, the company announced seven agreements with major wireless carriers and equipment companies such as Sprint PCS, Nokia, Motorola, and Arch Communications to deliver AOL features and services to millions of wireless consumers. AOL also initiated a new service to offer access to instant messaging over mobile phones and paging devices, and officially launched broadband AOL service under the name "AOL Plus" in April 2000.

Because of all of this, analysts have touted AOL as "an online 'must buy' in media circles . . . with AOL's ad revenues often exceeding the combined total of other major Internet

³⁶ See Lehman Brothers Report, at 2.

³⁷ See AOL Earnings Report.

³⁸ See Remarks of Bob Pittman, President and Chief Operating Officer, America Online, Inc., AOL Third Quarter Conference Call, April 18, 2000 <<http://corp.aol.com/conffy00q3.html>>.

³⁹ See AOL Earnings Report.

players.”⁴⁰ AOL members purchased \$3.9 billion in goods and services from online retailers in the March 2000 quarter, up from \$2.5 billion in the 1999 holiday season. On an annualized basis, AOL members are spending about \$15.6 billion on goods and services, 56 percent above 1999’s \$10 billion level. More than 40 percent of AOL’s members made an online purchase in March 2000 alone.⁴¹ As might be expected, given this level of growth, revenues were up 47 percent in the third quarter to \$1.8 billion, and revenues from advertising and commerce more than doubled to \$557 million. Net income was up 161 percent to \$271 million, and total revenues for AOL are expected to increase from an anticipated \$10.4 billion in 2001 to \$24.2 billion in 2005.⁴²

C. AOL HAS SUBSTANTIAL POWER IN SEVERAL INTERNET MARKETS

1. AOL Monopolizes The Instant Messaging Market

AOL owns the only two instant messaging services with a large base of subscribers: the AOL Instant Messenger (“AIM”) and Buddy List service, with 91 million registrants, and the ICQ service (acquired in 1998), with 62.4 million registrants, for a total of over 153 million instant messaging registrants.⁴³ By way of contrast, while exact figures are not available, the next largest company apparently has only about 8 million subscribers.⁴⁴ AOL has about a 90

⁴⁰ See Lehman Brothers Report, at 3.

⁴¹ See *id.* at 48.

⁴² See *id.* at 14.

⁴³ See AOL Earnings Report.

⁴⁴ See Comments of Tribal Voice, *In re Applications of America Online, Inc. and Time Warner Inc. for Transfers of Control*, CS Docket No. 00-30 (filed April 25, 2000).

percent share of the instant messaging market.⁴⁵ While the market is a new one, the value of this franchise is already about \$4.6 billion.⁴⁶

AOL's monopolization of this market is increasingly significant because instant messaging is rapidly evolving from a limited service, heavily used by teenagers and college students, to a technology platform for a wide array of services, including voice and video transmission used by a mass audience. Among these broader uses are, for instance, the furnishing of news, sports and financial information tailored to a particular recipient's requests.

Instant messaging will also be a prime component of the Interactive Television experience. In fact, AOL touts instant messaging, as well as chat rooms, as an integral component of AOL TV, envisioning a viewer communicating with an online Buddy while watching a football game, for instance. Thus, AOL's monopolization of the instant messaging market will be used as leverage to achieve market power in the Interactive Television market.

2. AOL Monopolizes The Online Service Provider Market

The OSP market consists of companies offering a package of ISP service and diverse Internet content.⁴⁷ Here, AOL has a monopoly market share – indeed, very few companies even try to offer a competing product. Earthlink, for instance, is essentially an ISP service with only a small amount of its own content. Conversely, popular web content portals, such as Yahoo, either do not offer ISP service or do so only on a small scale. Only AOL marries ISP service and Internet content in any meaningful way with significant subscribership. This is part of the reason for AOL's tremendous advertising advantage. While the average AOL member spends more

⁴⁵ *Id.*

⁴⁶ See Lehman Brothers Report, at 13.

⁴⁷ See generally United States v. Microsoft, 84 F.Supp.2d 9, 85-86 (D.D.C. 2000).

than 33 hours per month online and 85 percent of that time on AOL, the average visitor spends less than 73 minutes *per month* on Yahoo and 43 minutes *per month* on Excite.⁴⁸

3. AOL Dominates The ISP Market

AOL is clearly the dominant ISP in the United States and globally. AOL has achieved an approximately one-half share of the U.S. ISP market⁴⁹ and is expected to maintain that share despite the tremendous growth in the number of Americans subscribing to ISP service.⁵⁰ AOL dwarfs all other rivals. The second place ISP, Earthlink, even following its acquisition of Mindspring, still has only an 8 percent share.⁵¹ AOL's share is almost double that of the next ten providers combined.⁵² AOL has been able to maintain this share and its incredible growth rate due to huge sales and marketing expenditures. Since 1997, AOL has spent \$3.2 billion on sales and marketing, creating a "branding powerhouse."⁵³ Notably, AOL's member retention has improved steadily and is at the highest level in AOL's history, estimated at more than 80 percent.⁵⁴ AOL's share of the residential ISP market is even higher than of the overall ISP segment. It has been estimated recently at more than 50 percent.⁵⁵

⁴⁸ See Lehman Brothers Report, at 35.

⁴⁹ See YANKEE GROUP, AOL TIME WARNER MERGER IN THE CONTEXT OF CONSUMER ONLINE MIGRATION 6 (2000) ("Yankee Group Report").

⁵⁰ See Lehman Brothers Report, at 34.

⁵¹ See Yankee Group Report, at 6.

⁵² See Lehman Brothers Report, at 2.

⁵³ See Yankee Group Report, at 8.

⁵⁴ See Lehman Brothers Report, at 35.

⁵⁵ *Id.*

4. AOL Monopolizes Its Subscribers' Internet Experience

AOL carefully monitors and loudly proclaims the amount of its subscribers' online time spent within its "walled garden," that is, within the AOL site as opposed to other sites available on the World Wide Web. AOL has been increasingly successful at this strategy. In AOL's Third Quarter, AOL President Bob Pittman crowed that AOL's subscribers spent 85 percent of their time – an all time high – online within the AOL site.⁵⁶ In addition, the average amount of time AOL subscribers spend online grew to a record 64 minutes per day, increasing the significance of AOL's monopolization of its customers' time on the Internet.⁵⁷ This grip on subscriber time also will be increasingly significant as Interactive Television is rolled out, because the AOL experience will be a key component of that product.

With its dominant position in the ISP market, especially its residential component, its monopoly position in the OSP market, and its monopoly in the instant messaging business, it is no wonder that Merrill Lynch has reported that "AOL is well-positioned to become 'the operating system for consumer interactivity' - the interface through which the majority of consumers access the online world."⁵⁸ As AOL's CEO Steven Case puts it, "we expect to lead the transformation of the Internet into an 'everywhere and anywhere' experience."⁵⁹

⁵⁶ See AOL Earnings Report.

⁵⁷ See *id.*

⁵⁸ See Merrill Lynch, *AOL Time Warner: You've Got Upside!* 9 (2000) ("Merrill Lynch Report").

⁵⁹ See Remarks of Steve Case, Chief Executive Officer, America Online, Inc. AOL Third Quarter Conference Call, April 18, 2000 <<http://corp.aol.com/conffy00q3.html>>.

D. AOL OBTAINED AND HAS MAINTAINED ITS DOMINANT POSITION THROUGH EXCLUSIONARY CONDUCT

AOL has maintained its dominant position in Internet markets through a deliberate policy of exclusionary conduct. As AOL has gained further market power, these tactics increasingly have been successful in raising rivals' costs and, in fact, in excluding rivals altogether from certain markets.

1. Instant Messaging

An ongoing and blatant example of AOL's monopolistic behavior has been its campaign to exclude rivals from the instant messaging market. AOL's first move to eliminate competition to its AIM service was the 1998 acquisition of ICQ, a pioneering instant messaging service that had become the largest online communication network.⁶⁰ That acquisition secured for AOL what is currently a 90 percent share of the instant messaging market.

AOL has maintained its monopoly share by ruthlessly stamping out all attempts by rivals to interconnect with its service. This practice began in July, 1999 when Microsoft, Prodigy and Yahoo configured their competing instant messaging services so that their subscribers could send and receive instant messages to and from AOL's AIM registrants. Rivals developed the configurations needed to establish interconnectivity based on technology released by AOL. AOL's immediate response, however, was to block interoperability with such competing services.⁶¹ Microsoft tried several times to overcome AOL's blocking tactics but eventually gave up.

⁶⁰ See ICQ, *About the Company* (visited July 23, 2000) <<http://www.icq.com/company/about.html>>.

⁶¹ Rajiv Chandrasekaran, *Clash of the Titans Erupts Over AOL's Instant Messaging*, WASH. POST, July 24, 1999, at A1.

Disney has its own instant messaging service for children, Blastpad. While Disney would have liked to allow its Blastpad users to communicate via instant messaging with children registered with AOL's AIM service, the company decided not to try after seeing what had happened to Microsoft.

Subsequent efforts to establish interoperability with AOL's AIM services were made by, among others, Tribal Voice in the Fall of 1999, iCast at the end of February, 2000, and currently by Odigo. During June 2000, Odigo and AOL went through at least two rounds of temporary interconnection and then blocking, with AOL taking the position that it would continue to block Odigo's attempts at interoperability.⁶²

While it has been engaged in excluding its instant messaging rivals, AOL has proclaimed that it would work to help the industry develop a common system for instant messaging interoperability. Specifically, AOL pledged to work with the Internet Engineering Task Force ("IETF"). But in reality, AOL has engaged in a year-long stalling maneuver. In fact, AOL's CEO this March took the position that instead of an open standard, AOL wanted the market to evolve to one in which "everyone who wants to communicate with AOL members would use software 'licensed or approved by us.'"⁶³ AOL tried to get Disney to obtain a license for the AIM product and the AOL brand for instant messaging. Disney declined. Several companies have agreed to such licenses but at a stiff price: co-branding with AOL, loss of independence in the instant messaging area, and becoming subject to AOL's ability to change the terms of the license at will.

⁶² Jim Hu, *Odigo, AOL Fight over Instant Messaging Connections*, CNET NEWS.com, June 13, 2000.

⁶³ Ariana Eunjung Cha, *Foes of AOL Merger Take to Capitol Hill; Assurances Sought in Low-Profile Effort*, WASH. POST, Mar, 24, 2000, at E03 (quoting AOL Chairman and CEO, Steve Case).

Only recently, under the glare of merger-related publicity, has AOL submitted a proposal to the IETF; even that proposal was vague and general in content, not the specific technical protocols for implementation IETF had requested. As Ross Bagully, CEO of Tribal Voice, put it, the submission "is very high-level and esoteric . . . There is no hard timeframe of what AOL will do and when."⁶⁴

AOL has propounded several excuses for its obstructionist behavior. The company claims it is protecting its members' privacy and guarding them against spam. These claims, however, are specious. Interoperability could easily be achieved in a manner that would protect privacy and allow policing of spamming.

2. How AOL Tends Its Walled Garden: With Restrictive Contracts

The fact that AOL's users spend an astonishing 85 percent of their time online within the walled garden is not by accident. Rather, it is the product of a calculated and extensive course of restrictive dealings on AOL's part. AOL consistently demands that companies purchasing space on the AOL website desist from including links to websites outside the walled garden. Thus, AOL has created "content cul-de-sacs" to keep subscribers captive within the AOL Network. At times, AOL requires a commitment that no more than a set percentage of traffic at a site within the AOL network can be "diverted" from there via links to sites outside the AOL Network. In addition, AOL's competitors often are contractually precluded from achieving contact with AOL subscribers, and AOL may prevent the sale of, interaction with, download of, or access to competing products on the AOL site.

⁶⁴ Matt Richtel, *One Aspect of Messages on the Internet may be Delayed*, N.Y. TIMES, June 19, 2000, at C1.

3. AOL's Recent Exclusionary Tactics Directed At Rival ISPs

AOL's attempts to ensure that its subscribers stay within its walled garden are pursued by technological means as well as by contract. A recent example, which has given rise to a series of class action lawsuits, involves AOL's October, 1999 release of version 5.0 of its online access software.

According to these class action complaints,⁶⁵ installation of AOL 5.0 changes the user's communications configuration and settings to interfere with any non-AOL communications software. After installing AOL 5.0, apparently users have difficulty connecting to other ISPs or to run non-AOL e-mail programs, whether or not they respond "no" when asked during the installation process if they wanted to make AOL their "default provider." Thus, if an AOL subscriber wants to change to another ISP, it will find it difficult to do so because of the changes made to the user's system.

IV. TIME WARNER POSSESSES ENORMOUS MARKET POWER

A. TIME WARNER HAS SUBSTANTIAL MARKET POWER AT BOTH THE DISTRIBUTION AND PROGRAMMING LEVELS OF THE CABLE INDUSTRY

Time Warner enjoys market power, both as a cable MSO with local monopolies and as the owner of more popular cable programming networks than any other company. Time Warner's local cable franchises pass more than 21 million homes and serve approximately 20

⁶⁵ See Galaxy Internet Services, Inc., v. America Online, Inc., No. 0010651 GAO, (D. Mass. filed Apr. 3, 2000). See also Schmidt v. America Online, Inc., No. 00-139-WDS, (S.D. Ill. filed Feb. 23, 2000); North v. AOL, Inc., (Fla. Cir. Ct. filed Feb. 14, 2000); Wise v. America Online, Inc., No. 1:00 CV00282, (D.D.C. filed Feb. 11, 2000); Cofino v. America Online, Inc., No. 00-00547, (S.D. FLA. filed Feb. 9, 2000); CapuNet v. America Online (Md. Cir. Ct. filed Feb. 4, 2000).

percent of U.S. cable households, with nearly 13 million subscribers. With 34 cable clusters of more than 100,000 subscribers each,⁶⁶ Time Warner ranks as the second largest cable MSO.⁶⁷

Time Warner also is the largest distributor of cable programming networks in the United States, with a market share in excess of 40 percent.⁶⁸ It owns three of the five most watched cable programming networks (TBS #2; TNT #3; and Cartoon Network #5) as well as the leading cable news network, CNN, and the largest pay network, Home Box Office.⁶⁹ Time Warner's market power at the programming level led the Federal Trade Commission to place restraints on Time Warner's merger with Turner designed to prevent Time Warner from disadvantaging rival MVPD distributors.⁷⁰ In addition, Time Warner controls RoadRunner, one of two national cable modem broadband portals, serving 32 percent of broadband subscribers.

B. TIME WARNER'S LOCAL CABLE MONOPOLIES GIVE IT ENDURING MARKET POWER

Time Warner and other cable MSOs consistently have retained monopoly power in their local franchise areas. While cable's market share has declined very slowly over time (from 98

⁶⁶ See Time Warner Inc., *About Time Warner* (visited 7/17/2000) <<http://www.timewarner.com/corp/about/cablesys/index.html>>.

⁶⁷ See Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming, CS Docket No. 99-230, at Appendix (FCC Jan. 14, 2000) ("*Sixth Annual Video Competition Report*")

⁶⁸ See Time Warner Inc., Docket No. C-3709, at ¶ 31 (FTC Feb. 3, 1997).

⁶⁹ See Time Warner Inc., *About Time Warner* (visited 7/17/2000) <<http://www.timewarner.com/corp/about/cablenets/index.html>>.

⁷⁰ *In re Time Warner Inc.*, Analysis of Proposed Consent Order to Aid Public Comment, Docket No. C-3709, at 3-4 (FTC Feb. 3, 1997).

percent⁷¹ of the multichannel video programming distribution market in 1991 to 82 percent⁷² in 1999), its share of the market still is well over the level necessary to find market power.

While market share is indicative of monopoly power, other economic data clearly demonstrate cable's continuing monopoly power. Prices in monopoly cable franchise areas consistently are higher than in those few areas where there is a second cable provider. As recently as this June, the FCC found prices to be, on average, 19 percent lower in areas where a cable provider faced overbuild competition.⁷³ Earlier, the FCC and Professor Paul MacAvoy, in separate studies, found the cable industry to have persistent abnormally high q ratios, a mark of market power.⁷⁴

C. TIME WARNER IS THE WORLD'S LARGEST TRADITIONAL MEDIA COMPANY

Time Warner proclaims itself to be the leading media company in the world. It has significant positions in publishing, movie production, television production, and music creation and distribution, and controls a broadcast television network, in addition to its position as the largest cable programmer and second largest cable distributor.

- **Publishing.** Time Inc. is the largest U.S. consumer magazine distributor, and is bigger than the second and third largest distributors combined. The company publishes 36 magazines with 130 million readers and sells the

⁷¹ Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming, CS Docket No. 94-48, at ¶ 200 (FCC Sept. 28, 1994) ("*First Annual Video Competition Report*").

⁷² See *Sixth Annual Video Competition Report*, at App. C. If anything, the 82 percent figure understates cable's share because most of the non-cable MVPD percentage is accounted for by DBS service, which is proportionately much stronger in rural and non-cable areas.

⁷³ See 1999 Report on Cable Industry Prices, CS Docket 00-214, at ¶ 24 (FCC June 15, 2000).

⁷⁴ Tobin's q is the ratio of market valuation of assets to their replacement cost. If a q is above 1 persistently, it is an indication of long-run entry barriers. In 1990 MacAvoy found cable's q to be 4.3, see *1990 Cable Competition Report*, at App. E., and in 1994 the FCC staff calculated q at from 3.95 to 5.23, see *First Annual Video Competition Report*, at App. I, both very high numbers.

top three magazines in the U.S.: People, Sports Illustrated and Time.⁷⁵ Time Inc. accounted for 21.1 percent of total advertising revenues generated by consumer magazines in the U.S. in 1998.⁷⁶ Time Inc. also publishes books through the Warner Books and Little, Brown imprints, which had 31 books on the *New York Times* best seller list in 1998, and markets books directly through the Book-of-the-Month Club.⁷⁷

- **Music.** Time Warner produces, packages, manufactures and distributes music in more than 70 countries through leading labels such as Warner Brothers Records, Atlantic Recording, Rhino, and Elektra Entertainment. Time Warner is also the world's largest manufacturer of DVDs with a 38 percent market share.⁷⁸ The Warner Music Group's Joint Venture with EMI Music Group will merge the operations of the two leading music publishers (Warner Chappell alone controls more than one million copyrights) and two of the five dominant music distributors worldwide.⁷⁹
- **Motion Picture and Film Production.** "Warner Brothers is a global leader in the creation, distribution, licensing and marketing of movies, television programming, video and related products."⁸⁰ Warner Brothers is the largest supplier of television programming in the world.⁸¹ Altogether, Time Warner has a library of 5,700 feature films, 32,000 television titles and 13,500 animated titles.⁸²
- **Broadcast Television.** Warner Brothers also operates the WB Television Network, the only broadcast network to achieve a primetime ratings increase in the 1998-1999 season.⁸³

⁷⁵ See Lehman Brothers Report, at 28.

⁷⁶ See 1999 TIME WARNER FACTBOOK 8 ("Time Warner Factbook").

⁷⁷ See *id.* at 9.

⁷⁸ See Lehman Brothers Report, at 31.

⁷⁹ See Time Warner Factbook, at 12.

⁸⁰ See *id.* at 10.

⁸¹ See Lehman Brothers Report, at 29.

⁸² See Time Warner Factbook, at 10.

⁸³ See *id.*

D. THE BREADTH OF TIME WARNER'S HOLDINGS PLACES IT IN A UNIQUE POSITION TO DOMINATE THE INTERACTIVE SERVICES MARKET

No traditional media company begins to match Time Warner's collection of assets and brand names. As a leading analyst put it prior to the merger announcement:

Time Warner owns a portfolio of business that is unique in the media industry. It is the only company in the sector that will be both a combatant and an 'arms merchant' (i.e., content provider) in the coming war for digital audience share. Time Warner is the largest U.S. producer of television and live action movies, and its cable networks typically capture an aggregate audience in the U.S. which rivals that of the major broadcast networks in size ... Time Warner is almost perfectly hedged and can prevail in the digital decade under almost any scenario.⁸⁴

Perhaps Time Warner itself best sums up its own power and influence: "Time Warner Inc. is the world's leading media company. With an array of world-class brands ... Time Warner is helping transform the global information and entertainment landscape."⁸⁵

E. TIME WARNER'S EXCLUSIONARY CONDUCT

Time Warner has not been bashful about exercising the market power it possesses as a result of its extraordinary reach. Particularly troubling is how Time Warner has used the power of its local cable monopolies to maintain those monopolies and to extend them into adjacent markets.

1. Threats Regarding Disney's Free Satellite Dish Offer

Time Warner's most egregious recent attempt to suppress competition arose out of its retransmission consent negotiations with Disney, when it tried to punish Disney both privately and publicly for promoting satellite competition to its cable systems. Time Warner's behavior in

⁸⁴ See Morgan Stanley Dean Witter, *Multichannel Metamorphosis III: The Digital Decade*, April 6, 1999, at ii.

⁸⁵ See Time Warner Inc., *About Time Warner* (visited 7/17/2000) <<http://www.timewarner.com/corp/about/timewarnerinc/corporate/index.html>>.

this episode is noteworthy because it illustrates that its monopolistic culture is so deeply ingrained that, like AOL, it regards any attempt at competition as illegitimate.

During the course of the retransmission consent negotiations, Time Warner began a concerted private effort, which later turned public, to stop Disney from joining forces with DirecTV to promote satellite competition to its cable monopoly. Disney and DirecTV had launched a campaign in Houston, offering cable subscribers \$198 rebates to cover the cost of purchase and installation of a DirecTV satellite dish. This mere whiff of competition enraged Time Warner, which tried to persuade Disney to stop the dish campaign. When that failed, it threatened Disney, both publicly and privately. Disney was told that time Warner expected it to “pay” \$5,000, the going rate for a cable subscriber at the time, for each Time Warner subscriber who was signed up for a dish. Or, as a Time Warner Vice President put it to a trade magazine, in referring to the dishes distributed in Houston:

We said to [Disney’s personnel] that they need to take responsibility for the fact that they’ve taken action that, according to them, has cost us money . . . At the end of the day, we may very well have to assess what the costs have been to us in terms of lost customers in Houston and pass that along to them.⁸⁶

The same executive characterized Disney’s attempt to promote competition from satellite distributors as a “remarkable indication of bad faith,”⁸⁷ a “nakedly hostile act,”⁸⁸ an “indication

⁸⁶ Jon Lafayette & Doug Halonen, *Retrans bickering drags on*, ELECTRONIC MEDIA, May 1, 2000, at 4.

⁸⁷ Richard Huff, *We Get Back ABC, For Now, Time Warner, Disney Extend Deal Until July*, DAILY NEWS (New York), May 3, 2000, at 5.

⁸⁸ Jim Rutenberg, *Time Warner-Disney Fight Is a Boon for Satellite TV*, NEW YORK TIMES, at C6 (May 3, 2000).

that Disney is engaging in a campaign of destruction,”⁸⁹ an “assault on our business,”⁹⁰ and chastised Disney for “put[ting] the entire situation under a cloud which cannot be helpful in future negotiations. If Disney wanted to come to a mutually acceptable agreement with us, that is not the way to get this done.”⁹¹

2. Illegal Deletion Of ABC From Its Cable Systems

Related to Time Warner’s threats regarding Disney’s satellite dish offer is Time Warner’s illegal deletion of ABC owned and operated broadcast television stations from Time Warner cable systems on May 1, 2000. Time Warner went ahead with the deletion despite having received explicit permission in several letters from Disney to continue to carry the ABC network through May 24, 2000, the end of the “sweeps” period then underway. Time Warner’s response was to pull the plug on ABC at 12:01 a.m. on May 1 and to recklessly misrepresent to its captive cable subscribers that its illegal actions were the fault of Disney. ABC then filed an Emergency Petition at this Commission which promptly ruled time Warner’s action illegal.⁹²

As Chairman Kennard put it: “Time Warner Cable committed a clear violation of FCC rules . . . Unfortunately, millions of consumers paid the price. No company should use consumers as pawns in a private contract dispute.”⁹³ Ultimately, even AOL’s CEO, Steve Case,

⁸⁹ Richard Huff, *We Get Back ABC, For Now, Time Warner, Disney Extend Deal Until July*, DAILY NEWS (New York), May 3, 2000, at 5.

⁹⁰ *ABC Urges Cable Subscribers to Switch*, DETROIT NEWS, May 4, 2000, at B3.

⁹¹ Keith L. Alexander, *Time Warner agrees to air ABC for now*, USA TODAY, May 3, 2000.

⁹² *In re Time Warner Cable*, Emergency Petition of ABC, Inc. for Declaratory Ruling and Enforcement Order for Violation of Section 76.58 of Commission’s Rules, Or In the Alternative For Immediate Injunctive Relief In CRS 5543-C, Memorandum Opinion and Order in D.A. 00-987 (rel. May 3, 2000).

⁹³ *Statement of FCC Chairman William E. Kennard on Ruling in Time Warner Disney Dispute*, FCC NEWS, May 3, 2000.

admitted that Time Warner's illegal action was a colossal blunder, stating, in a very self-serving apology, that it was "[a] really dumb thing to do... it was particularly dumb because it was self inflicted."⁹⁴

3. Stripping Out Gemstar's Electronic Program Guide

Time Warner's removal of Gemstar's Electronic Program Guide ("EPG") signal from many of its cable systems is another example of Time Warner's ability, incentive, and willingness to leverage its cable monopoly to disadvantage competing content.

Gemstar's EPG is a free, on-screen programming guide that is carried over a television signal's vertical blanking interval ("VBI"), which is also used to transmit other public-service features such as closed captioning and V-chip coded information.⁹⁵

Time Warner's cable subsidiaries offer a competing EPG that is available in special EPG-equipped digital set-top boxes rented by Time Warner to consumers for an additional \$6.42 per month.⁹⁶

Over a period of two years, Time Warner has intentionally and systematically removed Gemstar's *Guide Plus+* program data from the broadcast VBI on its cable systems in nine different cities, some of which are targets for the planned launch of Time Warner's competing EPG.⁹⁷ To do so, Time Warner actually had to purchase special VBI-stripping equipment and

⁹⁴ Case Laments 'dumb' TW gaffe, AOL chief says Disney dispute heightened antitrust watch, HOLLYWOOD REPORTER, July 18, 2000.

⁹⁵ See Ted Hearn, *Gemstar, Op in VBI Feud*, MULTICHANNEL NEWS, Mar. 27, 2000, at 2.

⁹⁶ See Petition for Special Relief, *In re* Petition for Special Relief for Gemstar Int'l Group, Ltd, CSR Docket No. 5528-Z, at 8-10 (filed March 17, 2000).

⁹⁷ See *id.* at 13-16.

program it to remove particular lines of data from the VBI.⁹⁸ Time Warner has offered no plausible procompetitive justification for its exclusionary conduct, claiming only that “must-carry” is not applicable.

Recently, Time Warner has ceased stripping Gemstar’s signal, pending the outcome of the FCC proceeding or, more likely, because the FCC and FTC are currently scrutinizing its proposed merger with AOL. This episode demonstrates Time Warner’s incentive and ability to leverage its cable monopoly into a monopoly in the market for electronic program guides.

4. Refusal To Carry Independent Local News Channels

In many cities and states, local news channels have been started in recent years. Sometimes, as with New England Cable News, a cable MSO is involved as a partial or whole owner. In other cases, a local newspaper or an independent entity has set up the news channel. Generally, the local news channel has been able to obtain carriage on the cable systems in its area.

Time Warner is a major exception to this pattern. Time Warner itself has been very active in setting up its own local news channels. It owns such channels in New York City and Rochester, N.Y. and in Tampa and Orlando Florida.⁹⁹ It apparently plans to expand the concept to other areas where Time Warner has clusters of cable systems. For that reason, Time Warner has resisted carrying local news channels started by others.

For instance, in Columbus, Ohio, where Time Warner has a major cable system, it refused to carry a local news station for many months. Only after substantial adverse publicity

⁹⁸ See *id.* at 15.

⁹⁹ See Time Warner Factbook, at 15.

and during the course of the review of this merger did Time Warner finally agree to carry the local news station – but only on its limited distribution digital tier. Remaining without Time Warner cable distribution are local/regional news channels in Florida, Texas, New England and the Northwest.

5. Discrimination In Channel Placement

Where a channel is placed on a cable system is vitally important to its viewership and commercial viability. The most valuable locations are those at the lower end of the dial where the local VHF broadcast stations are located. A cable network may be willing to pay a substantial sum for a location on channels 2-13.

In New York City, VHF channels occupy seven of the lowest 13 channel positions (for interference reasons, the other six positions are left vacant for broadcast purposes, but there is no need to leave them vacant for cable transmission). Time Warner has discriminated in favor of its own programming and against non-affiliated programming in assigning the six available low position slots. Four of the six available slots in the nation's number one television market have been assigned by Time Warner to its own programming (TNT, TBS, CNN and New York One), a proportion far beyond the percentage of Time Warner-owned cable channels on the system. Significantly, TNT and TBS were moved to the lower channels after the Time Warner acquisition of Turner Broadcasting.

6. Current Exclusionary Behavior Is Part Of a Larger Historical Pattern

Time Warner's monopolistic, exclusionary acts discussed above are part of a much larger and long-lasting pattern of anticompetitive behavior, particular instances of which have included the following among others:

- Using its power as an MSO to foreclose the Showtime programming network from obtaining carriage on Time Warner-owned systems so as to benefit HBO;¹⁰⁰
- Attempting to deny Liberty Cable, a New York City competitor, distribution rights for the Court TV programming network;¹⁰¹
- Opposing NYNEX's video dial tone trial and entry in New York City;¹⁰²
- Opposing entry by overbuilders in every manner possible wherever it threatens Time Warner's monopolies. The most recent instance involves the application of Memphis Networkx, a joint venture of the city of Memphis's Light, Gas & Water Division and Aptus Networks, for regulatory approval to build a new broadband network in the Memphis, Tennessee area.¹⁰³

F. TIME WARNER'S EXERCISE OF MONOPSONY POWER

Just as Time Warner has used its monopoly power against rivals, so has it used its monopsony power against suppliers. A glaring example involving Disney demonstrates this propensity on the part of Time Warner. The Disney Channel began as a premium or pay service. Several years ago, Disney determined that it would better serve consumers to position the Disney Channel as a basic or non-pay service. Because cable operators share in the subscription revenue of a pay service, they may have some reluctance to move a channel from pay to basic. Nevertheless, over time, Disney reached amicable agreements with virtually all cable MSOs to move the Disney Channel to basic, with one notable exception: Time Warner.

Time Warner resisted moving the Disney Channel to basic. In some markets,

¹⁰⁰ See *Viacom Int'l Inc. v. Time Inc.*, 785 F. Supp. 371, 379-80 (S.D.N.Y. 1992).

¹⁰¹ See *In re Complaint of Liberty Cable Co., Inc. v. Courtroom Television Network*, CS-4242-P, at 1-3 (adopted Aug. 1, 1994).

¹⁰² See Kent Gibbons, *A VDT Trial Gets Spicy*, MULTICHANNEL NEWS, Nov. 7, 1994, at 51.

¹⁰³ See Comments of Memphis Light, Gas & Water Division, *In re Applications of America Online, Inc. and Time Warner Inc. for Transfer of Control*, CS Docket No. 00-30, at 1-3 (filed Apr. 26, 2000).

Disney was actually moved from basic to premium after Time Warner purchased a cable system from another MSO. The explanation for Time Warner's resistance to move the Disney Channel to basic is obvious: Time Warner's ownership of The Cartoon Network, which competes with the Disney Channel in the children's television genre. Ultimately, Disney was able to obtain Time Warner's agreement to gradually switch the Disney Channel to basic on the remainder of its systems, but only as a result of the public relations fiasco Time Warner faced for illegally dropping the ABC owned and operated broadcast television stations in May 2000.

G. AOL AND TIME WARNER'S PATTERN OF ABUSE THREATENS THE INTERACTIVE TELEVISION MARKET

As detailed above, AOL and Time Warner both have engaged in persistent and systematic anticompetitive behavior over the years. Their behavior, including refusals to deal, exclusions of competitors, and a leveraging of a monopoly position in one market to gain market power in a second market, is of the type that historically has been questioned by antitrust authorities. Such behavior is scrutinized particularly closely when engaged in by firms with the sweeping and entrenching market power exercised by both AOL and Time Warner. This propensity to engage in exclusionary conduct, including naked threats of retaliation, prohibitions against navigation links and competing advertising, and the deployment of special equipment to block competitors, is particularly troubling because the emerging market for Interactive Television will be vulnerable to all of these types of conduct.

V. INTERACTIVE TELEVISION IS RAPIDLY EMERGING AS THE FUTURE OF TELEVISION

Traditional television, computer technology and the Internet are converging to make possible a new and wholly distinct hybrid service, Interactive Television. As the President of AOL's Interactive Services Group puts it, "we've seen many industries get transformed by the technologies of the Internet, and we think the television business is teeing up to be next in